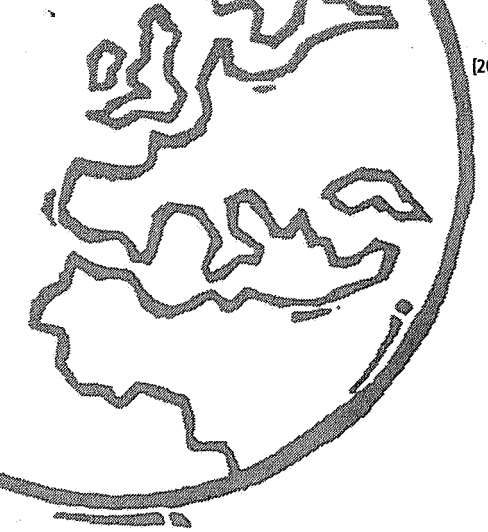
Should Europe harmonise environmental liability legislation?



Should Europe Harmonise Environmental Liability Legislation?

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INTRODUCTION

In this journal much attention has already been paid to the well-known White Paper on environmental liability, issued by the European Commission in February 2000. It has already devoted two articles to an overview of the contents of the White Paper and a critical analysis.[1]

More recently the regime proposed in the White Paper has also been analysed from an efficiency and insurability perspective.[2] However, so far most of these papers have accepted that the need to have a European-wide harmonised environmental liability regime is undisputed. Given the subsidiarity principle that is not that obvious at all. Moreover, the White Paper itself devotes much attention to the precise reasons for introducing an environmental liability regime at the European level. It is precisely that question, whether Europe should harmonise environmental legislation at all, that will be the central focus of this article. The reason we are interested in it is that we believe that the arguments advanced in the White Paper to promote action at the European level are not particularly convincing.

The methodology that we will use to address the need for the harmonisation of environmental liability legislation in Europe is the economics of federalism. This literature is interesting since it has extensively dealt with the optimal level of regulation within federal systems. The reader should therefore be aware that we merely provide 'one view of the cathedral'.[3] We do not deal with the question concerning the need for an environmental liability system. The mostly undisputed benefits of liability law as an instrument of both prevention and compensation have been stressed in a previous article.[4] This article also does not provide an assessment of the proposed liability regime in the White Paper; previous articles published in this review have already done this.[5] Moreover, it simply examines whether harmonisation of environmental liability legislation in Europe is desirable from an economic angle. We believe, however, that this economic approach is highly useful, since economists have also paid attention to the potential goals and economic effects of harmonisation. Thus, this economic methodology may allow us to show, as we believe, that the arguments for harmonisation provided in the White Paper are weak, at least on economic grounds. We will argue that this may even endanger the coming into being of a European-wide environmental liability system, since it can easily be shown, for example, that one of the arguments to justify this harmonisation (to have harmonised conditions of competition) is wrong on economic grounds. Therefore, even the proponents of a European-wide environmental liability regime should have an interest in the fact that the Commission should at least provide appropriate reasons for harmonisation in order to increase the likelihood of the adoption of such a regime. Indeed, one could well argue that there may be other, non-economic arguments for a harmonised environmental liability system such as, for example, the belief that this will lead to a higher degree of environmental protection than Member States would achieve when using national liability law. Our point is that the Commission should look carefully at the appropriate reasons for harmonising environmental liability since the reasons advanced so far in the White Paper seem doubtful.

Moreover, a focus on the correct reasons for harmonisation may also have important implications for

1 See P. Rice, 'From Lugano to Brussels via Arhus: Environmental Liability White Paper Published', [2000] *Environmental Liability*, at 39 to 45 and E. Rehbinder, 'Towards a Community Environmental Liability Regime: The Commission's White Paper on Environmental Liability', [2000] *Environmental Liability*, at 85 to 96.

2 M. Faure, 'The White Paper on Environmental Liability: Efficiency and Insurability Analysis', [2001] *Environmental Liability*.

3 See G. Calabresi and D. Melamed, 'Property Rules, Liability Rules and Inalienability: One View of the Cathedral', [1972] 85 *Harvard Law Review* (HLR) at 1089 to 1128.

4 See M. Faure, Note 2 above.

5 See the articles cited in Note 1 above.

the subject-matters one wishes to harmonise and for the methods of harmonisation chosen. It is fortunately not too late for such a critical review of the appropriate task of Europe as far as environmental liability is concerned, since the Commission announced that it would only publish its plans concerning further action with respect to environmental liability in autumn 2001. Meanwhile things have apparently advanced quickly, since on 30 July 2001 the Commission published a new working paper on prevention and restoration of significant environmental damage (available on its website), indicating the directions for a future environmental liability system. To a large extent the working paper builds on the liability approach of the White Paper and there seems to be an increased focus on the duty to clean up and on prevention. However, the White Paper remains an interesting policy document for further study, since it has paid attention to the need for harmonisation of environmental liability at the European level.

This article is structured as follows: first we look very briefly at the arguments advanced in the White Paper by the Commission for action at the European level; then we turn to the criteria for (de)centralisation advanced in economic literature, asking especially how these arguments relate to the need to harmonise environmental liability. Then we provide a critical assessment of the arguments advanced by the European Commission in favour of a European regime. We conclude by providing an interest group perspective and by formulating a few policy recommendations.

WHITE PAPER ON ENVIRONMENTAL LIABILITY

Purpose and History

In February 2000, the European Commission published the long-awaited White Paper on Environmental Liability.[6] In the White Paper the Commission describes its view on the key elements of a future Environmental Liability Directive. In the Commission's opinion, such a Directive would improve the implementation of the EC Treaty's grand principles of environmental policy incorporated in the EC Treaty (Article 174(2)), the preventive, precautionary and polluter pays principles. Furthermore, it would improve the enforcement of existing EC environmental laws, ensure decontamination and restoration of the environment, and better integration of the environment into other policy areas and improved functioning of the internal market. Liability should enhance incentives for more responsible behaviour by firms and thus exert a preventive effect.[7]

It took the Commission more than a decade before a proposal on an Environmental Liability Directive could be presented.[8] In 1989, the Commission proposed a Directive dealing only with liability for damage caused by waste;[9] however, the proposal was quickly abandoned. The Commission subsequently started to examine the possibilities of a broader liability regime covering environmental damage. In 1993, the Commission published a Green Paper on Remedying Environmental Damage,[10] which presented some broad notions on which an EC liability regime could be based and which was intended to initiate a public debate. For a short time, the Commission played with the idea of the EC joining the 1993 Council of Europe Lugano Convention, but this approach was rejected. According to the Commission the main differences between a Community Directive and Community accession to the Lugano Convention are that the scope of the Lugano Convention is too wide and gives too little legal certainty and that its definitions, especially in the field of environmental damage, are too vague. Community action can be better delimited and the regime for bio-diversity damage better elaborated in accordance with the relevant Community legislation. However, the Lugano Convention could provide an important source of inspiration for a future Community Directive.[11]

In November 1997, the Commission issued a working paper on environmental liability.[12] Compared with this paper, the White Paper finally published in February 2000 is less ambitious, and is vague in some elements. Although the publication of a White Paper is already a more formal

6 Commission of the European Communities, *White Paper on Environmental Liability*, COM (2000) 66 final, Brussels, 9 February 2000. See also L. Bergkamp, 'The White Paper on Environmental Liability', [2000] *European Environmental Law Review* (EELR), 105; P.E.A. Bierbooms and E.H.P. Brans, *Het EU Witboek Milieuaansprakelijkheid: de vage contouren van een toekomstig aansprakelijkheidsregime*, Milieu & Recht, July/August 2000 no. 7/8.

7 *White Paper on Environmental Liability*, Note 6 above, Executive Summary, at 7.

8 L. Bergkamp, Note 6 above, at 105 to 106 and P.E.A. Bierbooms and E.H.P. Brans, Note 6 above.

9 Proposal for a Directive on Civil Liability for Damage Caused by Waste, OJ C251/3 (1989); as amended COM (91) final OJ C192/6 (23 July 1991).

10 *Green Paper on Remedying Environmental Damage*, COM (93) 47 final, Brussels, 14 May 1993.

11 *White Paper on Environmental Liability*, § 5.1, at 25.

12 Commission of the European Communities, Working Paper on Environmental Liability, Brussels, 17 November 1997. For a comment on this draft see, for example, L. Bergkamp, 'A Future Environmental Liability Regime', [1998] EELR, 1998, at 200 to 204 and C. De Vries, 'Community Action on Environmental Liability', in L. Wiggers-Rust and K. Deketelaere (eds), *Aansprakelijkheid voor milieuschade en financiële zekerheid* (1999), at 141 to 147.

step towards EU legislation, it does not provide any guarantee that a Directive will finally be adopted. Nevertheless, for the purposes of this article, we will take the provisions of the White Paper as given and use it as a tool to test the economic theory of federalism.

Main Principles of the White Paper

The Commission suggests that an EC liability regime should be based on Article 175 of the Treaty. In accordance also with the subsidiarity and proportionality principles, the Directive should be a framework regime containing essential minimum requirements.[13] This framework Directive could be completed over time with other elements that might appear necessary on the basis of the experience gathered with its application during the initial period, called the step-by-step approach.[14]

The main features of the proposed liability regime that the Commission outlines in its White Paper are:[15]

- A regime that would not have retroactive effects (application to future damage only). The exclusion of the retroactivity is justified by reasons of legal certainty and legitimate expectation;
- Since the protection of health is also an important environmental objective, and for reasons of coherence, the proposed EC regime should cover both traditional damage (harm to health and property) and environmental damage (site contamination and damage to bio-diversity), which is currently not sufficiently covered by the Member States;
- The EC regime should be based on strict liability (this means that no fault by the polluter is required), when damage is caused by inherently dangerous activities, and fault-based liability for damage to bio-diversity caused by a non-dangerous activity.

Summarising, the White Paper suggests that the most appropriate option for an harmonised environmental liability regime would be a framework Directive providing for strict liability for damage caused by EC-regulated dangerous activities, with defences, covering both traditional and environmental damage, and fault-based liability for damage to biodiversity caused by non-dangerous activities. The details of such a Directive should be further elaborated in the light of consultations.

Arguments for Harmonisation: Harmonisation of Conditions of Competition

According to the subsidiarity principle,[15a] in areas where the EC does not have exclusive competence for jurisdiction, such as environment and hence environmental liability, the EC has to justify why it is in a better position than the Member States to set policy or legislation on a specific issue.

The European Commission has so far given a variety of reasons for legislative action at the European level with respect to environmental law. Although most Directives tend to have multiple reasons for their adoption,[16] the most important are:

- The *transboundary nature of the environmental problem* to be dealt with. Several Directives refer to the transboundary character of the pollution to argue for regulation at the European level. This is the case with, for instance, the Directive dealing with the discharge of dangerous substances into the aquatic environment;[17]
- The creation of *equal conditions of competition*. It is argued that harmonising conditions of competition is necessary for the functioning of the internal market. This argument, which is often referred to as the need to create a *level playing field* for industry in Europe, is not only used in environmental law, but is advanced to harmonise any kind of legislation within Europe.[18] The

13 For comments on this White Paper see, for example, G. Betlem, 'Commission adopts White Paper on environmental liability', [2000] *Tijdschrift voor Milieuaansprakelijkheid* (TMA), at 58 to 60 and P.F.A. Bierbooms and E.H.P. Brans, Note 6 above, at 182 to 188 and P. Rice, Note 1 above, at 39 to 45. Because with respect to some issues (such as causation or defences) no firm decisions have yet been taken Rehbinder is rather critical of the White Paper. He hopes for 'major improvement of the proposal'; see E. Rehbinder, Note 1 above, at 85 to 96; others are critical with respect to the proposals on action rights of NGOs, R. Hunter, 'European Commission White Paper Proposals on NGO Rights of Action: Wrongful Rights of Action', [2000] TMA, at 125 to 126.

14 *White Paper on Environmental Liability*, § 6, at 28.

15 Compare this to the general goals of environmental liability as stated in B. Jones, 'Deterring, Compensating and Remedying Environmental Damage: the Contribution of Tort Liability', in P. Wettenstein (ed.), *Harm to the Environment: the Right to Compensation and the Assessment of Damages* (1997), at 11 to 27.

15a This holds that the Community shall take action if and only in so far as the objectives of the proposed action cannot be sufficiently achieved by the Member States and can, therefore, by reason of the scale or effects of the proposed action, be better achieved by the Community (Article 5 EC Treaty).

16 For further details, see R. Van den Bergh, M. Faure and J. Lefevere, 'The Subsidiarity Principle in European environmental law: an Economic analysis' in E. Eide and R. Van den Bergh (eds), *Law and Economics of the Environment* (1996), at 128 to 131.

17 Directive 76/464, Discharge of Dangerous Substances into the Aquatic Environment, OJ 1976, L129/23.

18 Also the European Directive on Product Liability of 25 July 1985 was justified on the ground that differing liability rules in the Member States would hamper the conditions of competition. The considerations preceeding the Directive read: 'Whereas approximation of the laws of the Member States concerning the liability of the producer for damage caused by the defectiveness of his products is necessary because the existing divergences may distort competition and affect the movement of goods within the common market ...'

Directive on discharges of dangerous substances into the aquatic environment, mentioned above, was based on this 'harmonisation of conditions of competition' argument. It was argued that disparity between the provisions on discharge might create unequal conditions of competition and thus directly affect the functioning of the internal market.[19]

- A third reason advanced for European action with respect to environmental matters can be called a purely *ecological* one. There are a number of environmental Directives that aim at the protection of the 'European environmental and cultural heritage and human health'. One example is the Habitats Directive.[20]

Arguments Advanced by the Commission for the White Paper

The justifications mentioned above were also brought forward by the Commission in the White Paper in its argument in favour of a European environmental liability legislation. According to the subsidiarity principle,[21] which was mentioned above, in order to allow Community action. The Commission had to justify its claim in the White Paper that environmental liability could not effectively be dealt with by the Member States. The Commission accordingly dedicates a special section in the White Paper to the subsidiarity issue and the need for harmonised environmental liability legislation.[22]

In its paragraph on subsidiarity, the Commission states:

> ... the EC Treaty requires Community policy on the environment to contribute to preserving, protecting and improving the quality of the environment, and to protecting human health (Article 174(1)). This policy must also aim at a high level of protection, taking into account the diversity of situations in the various regions of the Community. It shall be based on the precautionary principle and on the principle that preventive action should be taken, that environmental damage should as a priority be rectified at source and that the polluter should pay (Article 174(2)).

According to the Commission 'these principles are currently not being implemented in an optimal way throughout the Community'.[23] The first reason the Commission offers is that there is a gap in most Member States' liability regimes concerning bio-diversity damage. Furthermore, according to the Commission, 'national legislation cannot effectively cover issues of transboundary environmental damage within the Community, which may affect, among others, watercourses and habitats, many of which straddle frontiers.' Therefore, the Commission concludes that an EC-wide regime is required in order to avoid insufficient solutions to transfrontier damage. An EC regime should aim at fixing the objectives and results, but the Member States should have freedom to choose the ways and instruments to achieve these goals.

A Closer Look at the Arguments

Thorough review of the White Paper thus reveals several arguments for harmonisation brought forward by the Commission in its introduction, sections 3, 5 and 6.[24] Let us first restate, in more detail, the arguments which the Commission uses to justify European action with respect to environmental liability.

Transfrontier damage

In the introduction to the White Paper, the Commission already indicates that harmonisation should be accepted under the subsidiarity principle, as Member States cannot adequately deal with transboundary environmental pollution. Section 6 of the White Paper dealing specifically with the subsidiarity issue states that a Directive would be necessary 'to avoid inadequate solutions to transfrontier damage'.[25] The Commission firmly states that national legislation cannot effectively cover transboundary environmental damage as various watercourses and protected habitats cross the borders of the Member States.

The polluter pays principle

Paragraph 3 deals with the advantages and hence the necessity of a European environmental liability legislation. First, the polluter pays principle is brought forward. In the Commission's view, the proposed liability regime would realise the three grand environmental principles enshrined in Article 174(2) of the EC Treaty: the polluter pays, the precautionary and the preventive principles. In particular, liability is viewed as a way of making the polluter pay: 'If polluters need to pay for damage caused, they will cut back pollution up to the point where the marginal cost of abatement exceeds the compensation avoided'.[26] The European Commission obviously refers to the economic theory of cost internalisation. As a firm will always try to

19 The same argument was made concerning other Directives as well; see R. Van den Bergh, M. Faure and J. Lefevere, Note 16 above, at 129.

20 Directive 92/43, OJ 1992, L206/7.

21 See on the issue of subsidiarity also C. Kimber, 'A Comparison of Environmental Federalism in the United States and the European Union', [1995] 54 *Maryland Law Review* (MLR), at 321 to 326.

22 *White Paper on Environmental Liability*, § 6, at 28.

23 *White Paper on Environmental Liability*, § 6, at 28.

24 See also L. Bergkamp, Note 8 above, at 106.

25 *White Paper on Environmental Liability*, § 6, at 28.

26 Ibid., § 3.1, at 14.

minimise its total costs, forcing the polluter to internalise the costs of pollution resulting from production, by obliging him to pay for the damage, would result in more precaution, and hence in prevention of environmental harm. Furthermore the Commission believes that liability may encourage investment in research and development (R&D) for improving knowledge and technologies.[27]

Decontamination and restoration of the environment and better implementation

In its plea for an EC environmental liability regime, the Commission raises two further arguments. A liability legislation would ensure decontamination and restoration of the environment and boost the implementation of, and compliance with, EC environmental legislation.[28]

Creating a level playing field

As the next argument, the Commission explains that an EC regime 'may contribute to creating a level playing field in the internal market'.[29] From this statement, it seems that the Commission is of the opinion that differences in the various national regimes may result in cost differences and thus in competitive advantages for companies in Member States with lax environmental liability regimes.

Principle of equal treatment

Finally, an argument that is rather hidden in paragraph 5.2, deals with the principle of equal treatment. Following the argument of transfrontier damage, the Commission argues that 'a system that addresses only transboundary problems would leave a serious gap where liability for biodiversity damage is concerned, since this is not covered at all by most Member States'. This could have as a consequence that purely national and cross-border cases will be treated differently, which could possibly violate the principle of equal treatment developed by the European Court of Justice.[30]

We will now turn immediately to the economic approach with the question: what does economics generally teach us about the necessity for harmonisation?

CRITERIA FOR (DE)CENTRALISATION OF ENVIRONMENTAL LIABILITY

Bottom up Federalism of Tiebout

The question as to whether regulation should be organised at a central (European or federal) level or at a more decentralised level (or, to put it in a more balanced way, what kind of regulations should be set at which level) has been addressed in the economics of federalism.[31] The starting point for the analysis is usually the theory of Tiebout (1956) about the optimal provision of local public goods.[32] Tiebout argued that when people with the same preferences cluster together in communities, competition between local authorities will, under certain restrictive conditions, lead to allocative efficiency. If there are, for example, in one community citizens with a high preference for sporting facilities and in other one a majority of citizens with a preference for opera, the first community will probably construct sporting facilities, whereas the second will probably provide an opera house. If someone living in the second community would prefer sporting facilities to the opera house, he could then move to the first community, which apparently provides services that better suit his preferences. The idea is that well informed citizens will move to the community that provides the local services that are best adapted to their personal preferences. Through this so-called 'voting with their feet', competition between local authorities will lead citizens to cluster together according to their preferences. In practice one can notice that different communities do indeed offer a variety of different services. The idea is that the citizen can influence this provision of local public goods either by influencing the decision-making (vote) or by moving (exit).

This basic idea applies not only to community services, but also, say, to fiscal decisions,[33] environmental choices[34] and even legal rules. It has been argued by Van den Bergh (1994) that competition between legislators will lead to legal systems competing each other, to provide legislation that corresponds best to the preferences of their citizens. Also Ogus (1999) argued that the various lawmakers in

27 Ibid.
28 Ibid., §§ 3.2 – 3.3, at 14.
29 Ibid., § 3.5, at 15.
30 Ibid., § 5.2, at 26.

31 This chapter is based on earlier research; see M. Faure, 'Regulatory Competition versus Harmonization in EU Environmental Law', in D. Esty and G. Geradin (eds), *Regulatory Competition and Economic Integration* (2001), at 263 to 286 and M. Faure, 'Product Liability and Product Safety in Europe: Harmonisation or Differentiation? [2000] 53 *Kyklos*, at 467 to 508.
32 For a discussion of this theory, see S. Rose-Ackerman, *Rethinking the Progressive Agenda, The Reform of the American Regulatory State* (1992), at 169 to 170.
33 See, for example, R.P. Inman and D.L. Rubinfeld, 'The EMU and fiscal policy in the new European community, an issue for economic federalism', [1994] 14 *International Review of Law and Economics* (IRLE), at 147 to 162; G. Kirchgässner and W.W. Pommerehne, 'Low-cost decisions as a challenge to public choice', [1993] 77 *Public Choice* (PC), at 107 to 116 and W.E. Oates, *Fiscal Federalism* (1972).
34 So W.E. Oates and R. Schwab, 'Economic Competition among Jurisdiction: Efficiency Enhancing or Distortion Inducing?' [1988] 35 *Journal of Public Economics* (JPE), at 333 to 354.

the nation-states would create competitive markets for the supply of law.

The idea therefore is that in an optimal world, citizens will cluster together in states that provide legal rules that correspond to their preferences. Well informed citizens, who may be dissatisfied with the legislation provided, could move (voting with their feet) to the community that provides legislation that corresponds best to their preferences. This idea, assuming that those different legal systems offer different legal rules, thus explains the variety and differences between the legal systems (Van den Bergh 1998). Moreover, it also shows that differences between the various legal rules of different countries should not necessarily be judged negatively, as is often the case in Europe today. The idea of competing legal systems can probably best be seen 'in action' in international private law where actors can chose the legal systems that best suits their needs in a choice of law regime.[35]

Obviously, assuming that competition between legal orders leads to allocative efficiency in the provision of legal rules, works only if certain conditions are met. One condition is that citizens have adequate information on the contents of the legal rules provided by the various legislators, in order to be able to make an informed choice. In addition, exit is often costly, so people may stay even if the (legal) regime does not suit their needs optimally.[36] Moreover, a location decision is obviously made under the influence of a set of criteria, in which the legal regime may not be decisive.[37] Usually job location and place of residence are so important that in reality there is often little left for people to choose.[38] Finally, as we will discuss below, this system of competition between legal orders works only if the decisions in one legal order have no external effects on others.

35 Although the choice for a particular legal regime may not always be related to the quality of the legal system but, for example, to the quality of the court or arbitration system. According to A. Ogus, 'Competition between national legal systems: a contribution of economic analysis to comparative law', [1999] 48 *International and Comparative Law Quarterly* (ICLQ) at 408, the latter explains the popularity of English law in choice of law clauses in contracts.

36 As A. Ogus, Note 35 above at 407, states, there should be no barriers to the freedom of establishment and to the movement of capital.

37 That is one of the reasons why B. Frey, 'FOCJ: Competitive Governments for Europe', [1996] 16 IRLE, at 315 to 327 and B. Frey and R. Eichenberger, 'To harmonise or to compete? That's not the question', [1996] 60 JPE, at 441 to 458, argue in favour of FOCJ: the choice for one legal or institutional regime should not be exclusive; there may be 'overlapping' jurisdictions depending upon the different functions.

38 S. Rose-Ackerman, Note 32 above, at 169.

In the economic literature, this Tiebout model is used to argue that, from an economic point of view, decentralisation should be the starting point, since competition between legislators will lead to allocative efficiency. Van den Bergh uses this theory as well to provide criteria for centralisation/decentralisation within the European Union.[39] Taking Tiebout as a starting point and assuming that competition between decentralised legislators will lead to an optimal provision of legal rules, the central question is: why centralise?

Van den Bergh therefore criticises a part of the current discussion in the European legal literature, which seems to focus on the question why there should be decentralisation (referred to by Van den Bergh as 'top down federalisation'). According to economic theory, that is the wrong question. Starting from Tiebout's model, there is reason to believe in what Van den Bergh calls a 'bottom up federalisation', assuming that in principle the local level is optimal, since the local level has the best information on local problems and on the preferences of citizens. Only when there is a good reason, should decision-making be moved to a higher level. Economic theory has indeed suggested that there may be a variety of reasons why the local level is not best suited to taking decisions and where central decision-making can lead to more efficient results.

These criteria for centralisation will now be applied to environmental liability. In particular, these criteria will provide information on whether a harmonised European environmental liability regime might be required.

Reasons for Centralisation

Transboundary character of the externality

Economics of scale argument

The Tiebout argument in favour of competition between local communities obviously works only if the problem to be regulated is indeed merely local. Once it is established that the problem to be regulated has a transboundary character, there may be an economics of scale argument to shift powers to a higher legal order that has the competence to deal with the externality over a larger territory. This corresponds with the basic insight that if the problem to regulate crosses the borders of competence of the regulatory authority, the decision-making power should be shifted to a higher regulatory level, preferably to an

39 R. Van den Bergh, 'Subsidiarity as an Economic Demarcation Principle and the Emergence of European Private Law', [1998] *Maastricht Journal of European and Comparative Law* (MJECL), at 129 to 152.

authority which has jurisdiction over a territory large enough to adequately deal with the problem.[40]

This argument in favour of centralisation could play a role with respect to environmental problems. It can be argued that these are certainly often transboundary.[41] The transboundary character of an externality is, within the European context, obviously an important argument for decision-making at the European level. Indeed, many environmental problems cross national borders. A great many of the environmental Directives fit into this economic criterion for community action. These include the regulation on the transboundary shipment of waste,[42] as well as many other Directives, which regulate pollution of a transboundary character.[43]

Therefore the most important reason for community action with respect to the environment is probably not the often stated argument of the harmonisation of conditions of competition, but simply the transboundary character of the pollution problem to be regulated. Many of the environmental Directives indeed deal with pollution problems which cross the borders of one single Member State. They can therefore be justified under this first economic criterion. This obviously does not necessarily imply that the contents of every Directive on this point has been efficient, nor that the instruments used to cure transboundary pollution have always been optimal.

Alternative solutions?

Some have warned, however, that the argument that centralised powers are necessary to deal with transboundary problems should not be accepted too easily.

First, Esty and Geradin have powerfully argued against an 'all or nothing' approach, meaning either all powers lie with the local authorities or shifting all powers to the central level. They have argued that the transboundary pollution problems can be dealt with via legal instruments other than centralisation, in other words via instruments which do not involve a change of the national environmental laws of a particular country.[44] One possibility is the external application of (domestic) high-standard country laws. Another one is the national enforcement of domestic laws with cross-border monitoring. In other words, the transboundary character of the externality may be an argument for co-operation, not necessarily for homogeneity of legal rules. However, Esty and Geradin admit that these alternative approaches have serious limitations as well and might not be effective remedies in all cases.[45]

Second, Cohen argued that Coasean bargaining between the polluting and the victim state may lead to negotiated agreements between them.[46] Therefore, Cohen argues that there is no *a priori* reason to centralise regulatory decision-making.[47] There might, however, be several reasons why the ideal solution from Coase's world might not be possible for solving transboundary pollution problems, for example in case of transboundary rivers such as the Rhine or the Meuse. First, Coase assumes that property rights are clearly defined.[48] Although there are some indications in international environmental law on this point, it might not be certain what the legal rule is: the right to pollute or the polluter pays. This uncertainty concerning the assignment of property rights might endanger negotiations. Second, adequate information is needed both on the consequences of pollution and on the possible abatement techniques[49] and third, there may be no strategic behaviour. Finally, parties need to have the possibility of enforcing a negotiated agreement. In that respect the EC framework might have several advantages. The EC offers an institutional framework that provides legal instruments to enforce an agreement. Moreover, the EC regulatory framework might fix the

40 Compare A. Ogus, Note 35 above, at 414 and C. Kimber, Note 21 above; D. Esty, 'Revitalizing Environmental Federalism', [1996] 95 *Michigan Law Review*, at 625 and S. Rose-Ackerman, Note 32 above, at 164 to 165. See also A. Arcuri, 'Controlling Environmental Risk in Europe: the Complementary Role of an EC Environmental Liability Regime', [2001] TMA, at 41 to 42.

41 See equally W. Oates and R. Schwab, Note 34 above, who also argue that as long as the effects of pollutants are confined within the borders of the relavant jurisdictions, local authorities will make socially optimal decisions of environmental quality.

42 Regulation 259/93 of 1 February 1993, *OJ*, 1993, L30.

43 This is certainly the case as well for Directive 76/464 on the Discharge of Dangerous Substances into the Aquatic Environment. For other examples, see R. Van den Bergh, M. Faure and J. Lefevere, Note 16 above, at 131 to 132.

44 See D. Esty and D. Geradin, 'Environmental Protection and International Competitiveness. A Conceptual Framework', [1998] 32/3 *Journal of World Trade* (JWT), at 5 to 46 and D. Esty and D. Geradin, 'Market Access, Competitiveness and Harmonization: Environmental Protection in Regional Trade Agreements', [1997] 21 *Harvard Environmental Law Review* (HELR), at 265 to 336, in which they provide an interesting overview of the various legal instruments to deal with harmonisation and apply this in the NAFTA and in the European context. See also M. Trebilcock and R. Howse, 'Trade Liberalization and Regulatory Diversity, Reconciling Competitive Markets with Competitive Politics', [1999] 6 *European Journal of Law and Economics* (EJLE), at 5 to 37.

45 D. Esty and D. Geradin, Note 44 above, at 34 to 35.

46 See also R. Van den Bergh, 'Economics in a legal strait-jacket: the difficult reception of economic analysis in European Law' (paper presented at the workshop Empirical Research and Legal Realism. Setting the Agenda, Haifa, 6–9 June 1999).

47 M. Cohen, Commentary, in E. Eide and R. Van den Bergh (eds), *Law and Economics of the Environment* (1996), at 167 to 171.

48 Which M. Cohen, Note 47 above at 168 to 169, mentions as well.

49 Ibid., at 168.

property rights. Also, the fact that Member States within the EC framework are repeat players (the one who is an injurer today may be a victim tomorrow) may cure the risk of strategic behaviour. If one also looks at the practice of transboundary pollution in Europe, one may argue that indeed the EC approach has achieved far better results so far than all the attempts towards bilateral agreements. EC Directives on (transboundary) pollution of waters provided Dutch victims of Belgian pollution of the river Meuse with a powerful tool to force the Belgians to reduce pollution,[50] a result which could probably never be achieved through the protracted negotiations between the two countries. Thus, the EC has undoubtedly played an important role as far as providing remedies against *transboundary* pollution is concerned.

However, Van den Bergh has demonstrated that in some cases, more particularly in the area of private law, European law cannot be considered an effective remedy to the interstate externality problem.[51] In some cases European law goes further than is needed to cure transboundary externalities; in other cases less far reaching legal instruments than total harmonisation could be used to remedy the problem.[52] There is, in other words, always the risk that the cure may be worse than the disease. The first issue relates to the problem that European Directives often cover both local and Community-wide pollution, without making a distinction between regional and interstate pollution.[53] The second point is that in some cases transboundary externalities may also be internalised by national law. The simple fact of transboundary effects is therefore not sufficient to justify European law-making.[54] Nevertheless, there can indeed be cases where one can hold that decentralised legal rule-making will not be able to remedy the transboundary externality.

Applied to environmental liability

In some cases the EC considers the transboundary character of a problem as a sufficient justification for centralised rule-making without differentiating between local and transboundary pollution.[55] Moreover, much in the environmental Directives also deals with relatively 'local' problems that do not cross national borders. This seems to be the case as well for environmental liability. Many pollution cases giving rise to liability are confined within the borders of one country. Moreover, even if there is transboundary pollution, other remedies could be applied (for example, via international private law) that do not go as far as the total harmonisation. Note that this 'transboundary externality' argument is a totally different one in a product liability case, since the likelihood of products affecting international trade is obviously quite large.[56] For environmental liability there would only be a case for centralisation if the central rules were to apply only to transboundary pollution and the question would only arise if this problem could not be remedied by less far-reaching means. However, the European environmental liability regime as proposed in the White Paper supposedly applies to 'damage to biodiversity', which is not necessarily transboundary. The question therefore arises whether other economic reasons can be found for European environmental liability legislation in those cases where the effects of pollutants are confined within the borders of the relevant Member States , for example in the case of soil pollution.[57]

Race for the bottom

There exists a second economic argument for a centralised regulation of environmental problems. The risk of destructive competition, known as a 'race for the bottom' between countries that could emerge to attract foreign investments with low environmental standards. As a result of this, a prisoner's dilemma could arise, whereby countries would fail to enact or enforce efficient legislation. It would mean that local governments would compete with lenient environmental legislation to attract industry.[58] The result would be an overall reduction of environmental quality below efficient levels. This should correspond with the traditional game-theoretical result that prisoner's dilemmas create inefficiencies. Centralisation could be advanced as a remedy for these prisoner's dilemmas.

This 'race for the bottom' argument, that competition among jurisdictions for economic activity will be 'destructive', corresponds to some extent with the above-mentioned Commission argument in the White Paper that the creation of harmonised conditions of competition is

50 See M. Pâques, 'Effet direct du droit communautaire, interprétation conforme et responsabilité de l'Etat en général et en matière d'environnement', in J. Van Dunné (ed.), *Non-Point Source River Pollution; The Case of the River Meuse* (1996), at 89 to 139. See, for the case of the river Rhine, J. Van Dunné, *Transboundary Pollution and Liability: the Case of the River Rhine* (1991).

51 R. Van den Bergh, Note 39 above, at 143.

52 Ibid., at 144 to 145.

53 So R. Van den Bergh, Note 46 above, at 10.

54 R. Van den Bergh, Note 39 above, at 144 to 145.

55 See, for instance, Directive 74/464, which regulates discharges of dangerous substances into the aquatic environment for both transboundary rivers and local pounds.

56 See R.M. Ackerman, 'Tort Law and Federalism: Whatever Happened to Devolution?' [1996] *Yale Law and Policy Review*, at 429 to 463 and G.T. Schwartz, 'Considering the proper federal role in American tort law', [1996] 38 *Arizona Law Review*, at 917 to 951.

57 The regime as proposed in the White Paper should typically apply to soil pollution.

58 Compare S. Rose-Ackerman, Note 32 above, at 166 to 170.

necessary to avoid trade distortions. The trade argument is traditionally used to harmonise legislation of the Member States in a variety of areas. Simply stated, the argument is that complying with legislation imposes costs on industry. If legislation is different, these costs would therefore differ as well and conditions of competition within the common market would not be equal. The argument apparently assumes that total equality of conditions of competition is necessary for the functioning of the common market. 'Levelling the playing field' for European industry remains the central message.

The 'race for the bottom' argument has had several supporters as well as opponents in North American scholarship. Law and economics scholars tend to stress the benefits of competition between states and point at the dangers of centralisation,[59] whereas some legal scholars tend to attach more belief to the 'race for the bottom' rationale for centralisation in environmental matters.[60] In Europe these issues are rarely discussed in the context of the 'race for the bottom' but rather in the European community dogma of 'levelling the playing field to avoid distortions of competition'. This somewhat confuses the debate. The 'harmonisation of conditions of competition' argument could either be interpreted narrowly in 'race for the bottom' terms or more broadly as a general argument to harmonise all kinds of rules and standards. The latter is the usual interpretation in Europe. Let us look at both interpretations more closely and see how they relate to the area of environmental liability.

Risk of the bottom versus common market

The traditional European argument claims that any difference in legislation between Member States might endanger the conditions of competition and therefore justifies the harmonisation of legal rules. This argument seems particularly weak. From an economic point of view, the mere fact that conditions of competition differ does not necessarily create a 'race for the bottom' risk. There can be differences in marketing conditions for a variety of reasons, and if the conditions of competition were indeed totally equal, as the argument assumes, there would also be no trade according to the theory of specialisation.

Also, Europe has developed an elaborate set of rules, which guarantee, *inter alia,* a free flow of products and services[61] and thus contribute to market integration without the necessity to harmonise all rules and standards.[62] In this respect one can think of the case law of the European Court of Justice with respect to the free movement of goods versus environmental protection.[63] This shows that the goal of market integration can be achieved via (other) less far-reaching instruments than total harmonisation[64] which can equally remove barriers to trade.

Hence, one should make a distinction between the political ideal of creating one common market in Europe on the one hand and the (economic) 'race to the bottom' argument on the other hand.[65] This political goal of market integration may as such be questioned on economic grounds[66] and may justify the need for rules aiming at a reduction of trade restrictions such as, for example, a harmonisation of product standards.[67] The problem in environmental law is that initiatives in that area also aim at a harmonisation of process standards 'to harmonise conditions of competition'. That seems questionable on efficiency grounds.[68] What can be said about this 'harmonisation of conditions of competition' argument either in its 'race for the bottom' or in its 'Common Market' version?

From an economic perspective, differences in the conditions of competition only pose a problem if it is clear that environmental costs would be considerably different between Member States and that these differences would lead to relocation of firms to the Member State with the

59 See especially with applications to environmental law R. Revesz, 'Rehabilitating Interstate Competition: Rethinking the Race for the Bottom Rational for Federal Environmental Regulation', [1992] 67 *NewYork University Law Review* (NYULR), at 1210 to 1254 and R. Revesz, 'Federalism and Interstate Environmental Externalities', [1996] 144 *University of Pennsylvania Law Review* (UPLR), at 2341 to 2416.

60 See D. Esty and D. Geradin (1997) and (1998), Note 44 above.

61 See Articles 28 to 30 of the Treaty (formerly Articles 30 to 36).

62 See generally on the potential conflict between free trade and environmental protection, D. Esty, 'Economic Integration and the Environment', in N. Vig and R. Axelrod (eds), *The Global Environment* (1999), at 190 to 209.

63 For an overview of this case law see J. Lefevere and M. Faure, 'Introduction to European Environmental Law', in T. Kegels (ed.), *Shipping Law faces Europe: European Policy Competition and Environment* (1995), at 93 to 107 and M. Trebilcock and R. Howse, Note 44 above, at 21 to 28.

64 See also D. Esty and D. Geradin, Note 44 above at 296 to 299 and A. Ogus, *Regulation, Legal Form and Economic Theory* (1994), at 177 to 179.

65 See also R. Revesz, 'Environmental Regulation in Federal Systems', in *Yearbook of European Environmental Law* (2000), at 24 to 27, who equally argues that these are separate points which should be distinguished.

66 See R. Van den Bergh, Note 46 above.

67 These were the result of Directives issued as a consequence of the so-called 'Single Market Initiative'. See D. Vogel, *Trading Up: Consumer and Environmental Regulation in the Global Economy* (1995). See on the need to harmonise product safety, M. Faure, Note 31 above, at 467 to 508.

68 This is also criticised by R. Revesz, Note 65 above.

lowest standards.[69] In that case, the so-called race for the bottom argument, referred to in environmental cases as the 'pollution haven' hypothesis, might be an argument in favour of centralisation.[70] The question therefore arises whether there is empirical evidence that states can indeed attract industry by lenient environmental standards.

Empirical evidence of pollution havens

Empirical evidence to uphold this 'race for the bottom' rationale is rather weak. Repetto argues that pollution control costs are only a minor fraction of the total sales of manufacturing industries.[71] Moreover, Jaffe, Peterson, Portney and Stavins[72] argue that empirical evidence shows that the effects of environmental regulations are 'either small, statistically insignificant or not robust to tests of model specification'. They argue that the stringency of environmental regulations might have some effect on new firms in their decision to locate for the first time,[73] but this will not induce existing firms to relocate. They equally argue that other criteria such as tax levels, public services and the unionisation of the labour force have a much more significant impact on the location decision than environmental regulation. Recently this empirical evidence has been somewhat contradicted by Xing and Kolstad,[74] who argue that the laxity of environmental regulations in a host country is a significant determinant of foreign direct investment by the US chemical industry. They claim that the more lax the regulations, the more likely the country is to attract foreign investment, although this somewhat weakens the evidence presented by Jaffe, Peterson, Portney and Stavins[75] as far as the location of new firms outside the United States is concerned.

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This material, therefore, weakens the prisoner's dilemma argument. Moreover, it has also been argued that as far as environmental standards are concerned, it is not at all clear that there will be a race for the bottom. There is also some evidence that Member States try precisely to strive for high environmental standards, even if this imposes extra costs or burdens on their industry. Some countries may therefore be more involved in a 'race for the top' instead of a 'race for the bottom'.[79] One could also question whether European law is at all able to remedy a real 'race for the bottom' risk, given the enforcement deficit.

'Race for the bottom' in environmental liability?

All these arguments apply to the area of environmental liability as well. It is doubtful whether within Europe Member States would be able to engage in a game in which they would strive for low level environmental liability in order to attract industry. There is no proof of such a destructive competition towards lower liability standards and this risk is, moreover, not very realistic. Indeed, as indicated, one can doubt whether environmental liability plays a significant role in attracting or repulsing business to or from a given state. Other elements may be far more important than the level of environmental liability in businesses' location decisions. Moreover, if environmental liability were to have any effect as far as the race for the bottom is concerned, it is even more likely that states would wish to protect victims of environmental pollution instead

69 See equally R. Revesz, who argues that given the weaknesses of the 'harmonisation of conditions of competition' argument 'it is not surprising that recent European scholarship has sought to recharacterize the quest for harmonization in race to the bottom terms'.

70 Although Esty and Geradin have rightly pointed at the fact that a whole variety of legal instruments exists which may remedy the problem, whereby the total harmonisation of standards would be the most far reaching: Note 44 above at 282 to 294.

71 R. Repetto, *Trade and Sustainable Development*, UNEP, Environment and Trade Series.

72 A. Jaffe, S. Portney and R. Stavins, 'Environmental Regulation and the Competitiveness of US Manufacturing: What does the Evidence tell us?', [1995] 33 *Journal of Economic Literature* (JEL), at 132 to 163.

73 See D. Esty and D. Geradin, Note 44 above, at 12 to 15.

74 Y. Xing and C. Kolstad, 'Do Lax Environmental Regulations attrack foreign Investment', 16-95 (working paper in Economics, University of California, 1995).

75 See Note 72 above.

76 R. Repetto, Note 71 above.

77 A. Jaffe, S. Portney and R. Stavins, Note 72 above, at 132 to 163.

78 See D. Esty and D. Geradin, Note 44 above, at 12 to 15.

79 So R. Van den Bergh, M. Faure and J. Lefevere, Note 16 above, at 141 to 142. Ogus argues that there may be benefits to firms to be located in a high standard Member State, since this may generate technological improvements and thus competitive advantages; that may explain 'race for the top' (Note 35 above, at 415). See, generally, D. Vogel, Note 67 above, at 13 to 14.

of corporate interests. Indeed, a lenient environmental liability legislation may well run counter to the states' interests since it would limit, for example, the possibilities of recovering soil clean-up costs from liable polluters. If there is any effect at all one can therefore expect a 'race for the top' rather than a 'race for the bottom' in the area of environmental liability. This would enable states to recover, say, costs for the clean-up of (domestically) polluted soils from foreign polluters as well.

Levelling the playing field

Let us now turn to the other – legal – interpretation of the 'race for the bottom' argument. It should be stressed that this European argument that markets would be distorted without a harmonisation of conditions of competition, is not only constantly repeated in a stereotypical way, but its validity is hardly ever questioned. The argument as it is usually presented in Europe, cannot, as was stated above, be fitted into the economic criteria for centralisation, since it suggests that removing any difference in legal systems would be necessary to cure the 'race for the bottom' risk, which is neither supported by economic theory, nor by empirical evidence. Also, even if one took the (political) 'common market' goal as the starting point and environmental regulations were harmonised on that ground, this would still not create a level playing field since differences in, for example, energy sources, access to raw materials and atmospheric conditions would still lead to diverting marketing conditions.[80]

There is, in addition, a strong counter-argument, in that there are many examples showing that economic market integration is possible (without the distortions predicted by the race for the bottom argument) with differentiated legal orders. Public choice scholars have often advanced the Swiss federal model as an example where economic market integration goes hand in hand with differentiated legal systems.[81] It is apparently possible to create a common market without a total harmonisation of all legal rules and standards.[82]

These arguments therefore weaken the prisoner's dilemma argument in the field of environmental law both in its 'race to the bottom' form and in the (disguised) way it is presented in the European debate. The European argument that any difference in legal rules between the Member States would endanger market integration and that therefore a harmonisation of law is needed in order to harmonise conditions of competition[83] is too general, unbalanced and not supported by economic theory. Differences between legal systems of Member States may, from an economic point of view, constitute a problem if this resulted in an inefficient race for the bottom. But the empirical evidence available suggests that this may not be a serious risk in the environmental field. Even if differences in the stringency of environmental law exist between Member States, this will generally not lead companies to relocate to 'pollution havens' within Europe. The least one can argue is that if the European Commission were to use a 'race for the bottom' rationale for centralisation, it should prove that without centralisation in the specific field a risk of destructive competition would emerge.[84] The debate in Europe has, so far, never focused on that question,[85] since it was always argued that any harmonisation of legal rules was necessary to achieve market integration, which obviously confuses the debate.

The same applies for the area of environmental liability. It is indeed possible to create a common market without a total harmonisation of all legal rules. The goal of market integration should not necessarily be achieved via this far-reaching instrument of total harmonisation. This would only justify, for example, general safety standards that aim at avoiding pointless incompatibilities which could create barriers to trade and distortions of competition within the internal market. The latter argument can, however, not justify a harmonisation of rules of private law such as environmental liability. Finally, attempts which have been undertaken so far to harmonise rules of private law, for example in the area of product liability, have not proved to be able to achieve a total harmonisation of marketing conditions.[86]

Transaction costs

Does harmonisation reduce transaction costs?

There may, however, be one final economic argument in favour of harmonisation, based on transaction costs

80 So R. Van den Bergh, Note 46 above, at 10.

81 B. Frey, 'Direct Democracy: Politico-Economic Lessons from Switzerland', [1994] 84 *American Economic Review*, at 338 to 342.

82 See equally R. Revesz, Note 65 above, at 24 to 27.

83 See the formulation in the preamble to the Products Liability Directive, cited in Note 18 above.

84 In that case there may seriously be a valid argument for an intervention by Brussels. Compare – in the US context – the remark by S. Rose-Ackerman, Note 32 above, at 173: 'If state and local laws seem designed to protect local business rather than reflect genuine differences in tastes across jurisdiction, the federal government should take a hard look to determine the possible interference with interstate commerce.'

85 See equally D. Esty and D. Geradin, who argue that the risk of a regulatory race to the bottom for environmental reasons has not been a major issue in the EC (Note 44 above, at 308).

86 M. Faure, Note 31 above.

reduction.[87] This argument is often advanced by European legal scholars pleading for harmonisation of private law in Europe, and is based on the argument that differences in legal systems are very complex and only serve Brussels law firms.[88] This argument cannot be examined in detail here.[89] It is obviously too simple to state that a harmonised legal system is always more efficient than differentiated legal rules because of the transaction costs savings inherent in harmonised rules.[90] This argument neglects the fact that there are substantial benefits from differentiation whereby legislation can be adapted to the preferences of individuals.[91] Moreover, given the differences between the legal systems (and legal cultures) in Europe the costs of harmonisation may also be huge, if not prohibitive.[92] The crucial question, therefore, is whether the possible transaction costs savings of harmonisation outweigh the benefits of differentiated legal rules. There is little empirical evidence to support the statement that transaction costs savings could justify a European harmonisation of all kinds of legal rules. Moreover, the transaction cost savings are likely to be relatively small.[93]

Does the White Paper reduce transaction costs?

If one addresses the question whether the regime proposed in the White Paper could achieve a reduction of transaction costs one would have to assess whether it can create a uniform regime and provide a legal certainty which would reduce transaction costs. That is highly doubtful.

Indeed, there is one particular point of concern about the regime proposed in the White Paper which may endanger the uniformity and increase transaction costs. This has to do with the balanced approach chosen in the White Paper which may make a future liability regime highly complex. A scheme provided in the White Paper itself [94] makes clear that the proposed regime is not only very balanced, but also very complex. Indeed, as the summary shows, the applicable regime will depend on the type of damage (traditional damage, contaminated sites or damage to biodiversity) and in addition on the type of activity (dangerous or not). Moreover, the White Paper argues that it focuses on damage to biodiversity, since most existing Member States' environmental liability regimes would not cover that type of damage. The question, however, arises whether that is generally true; Member States certainly have rules on traditional damage and contaminated sites.

This entails a risk of increased legal complexity, which could lead to cases whereby different legal regimes (different European and national regimes) apply to various types of damage, resulting from a single pollution case. That would obviously create legal uncertainty and may hence endanger the reduction of transaction costs.

To a large extent, this is due to the fact that until now the White Paper has not addressed the question how the different regimes proposed should be combined, if, for example, a non-dangerous activity causes damage to the soil, to human health but to biodiversity as well. A future regime should definitely better clarify how these (European and national) rules apply to specific cases if one would really wish to reduce transaction costs.

The transaction costs argument could, however, play a role in justifying so-called negative harmonisation, which aims at a co-ordination of, say, product standards to stop states hindering a free flow of products and services.[95] This type of co-operation between states can reduce transaction costs, but does not necessitate a homogenisation of process standards, which is often the goal in environmental law.

The conclusion therefore is that the economic arguments to harmonise environmental rules with respect to problems which are not transboundary are relatively weak. Nevertheless, many European Directives deal with problems which are not typically transboundary (for example, drinking water or bathing water), and for which the European competence is therefore difficult to fit into the economic framework. The question, however, arises whether a non-economic argument can be advanced for regulation at the European level.

The European heritage argument

Can an argument be found to protect the environment at the European level as such? The protection of habitats and entire ecosystems come to mind. This is of particular importance since the White Paper focuses precisely on

87 A somewhat related but different argument relates to economics and diseconomics of scale in administration: see S. Rose-Ackerman, Note 32 above, at 165 to 166.

88 This is one of the arguments made by the Danish scholar Lando in favour of harmonised private law. O. Lando, 'Die Regeln des Europäischen Vertragsrecht', in P. Müller-Graff (ed.), *Gemeinsames Privatrecht in der Europäischen Gemeinschaft* (1993), at 473 to 474.

89 It is further developed and criticised in a recent paper by R. Van den Bergh, Note 39 above, at 129 to 152.

90 Compare S. Rose-Ackerman, Note 32 above, at 172, who argues that uniform federal regulation may reduce search costs and tends to produce a more stable and predictable jurisprudence.

91 R. Mendelsohn, 'Regulatory Heterogeneous Emissions', [1986] 13 *Journal of Environmental Economics and Management* (JEEM), at 301.

92 That point has especially been made by B. Legrand, 'The impossibility of "legal transplants"', [1997] MJECL at 111.

93 So R. Van den Bergh, Note 39 above, at 146 to 148.

94 Included in the appendix to this article.

95 See D. Vogel, Note 67 above, at 52 to 55.

damage to biodiversity. A traditional example is the question whether there should be any European jurisdiction to protect an imaginary turtle which has, say, only one habitat, which is in Greece. The traditional economic argument in such a case would be that since the problem is merely local, the Greek population should decide whether or not to protect the Greek turtle. An attempt in the direction of an economic argument for European competence has been made by Wils, who classifies the protection of endangered species as justified by the fact that this endangerment causes 'psychic spill-overs'.[96] The argument then goes that the endangerment of the Greek turtle would also harm the interests of, say, a Dutch citizen living in Maastricht who would suffer a psychic spill-over from the fact that the Greek turtle was endangered.[97] According to this view, the externality would be considered transboundary (although the turtle only lives in Greece) and there would, again, be an economic rationale for centralisation.[98] Maybe this argument still holds for turtles or for Italian nature parks, whose well-being also affects other European citizens.[99] But what about a European Directive, regulating liability of soil pollution by a certain plant and regulating clean-up standards?

Differentiation according to preferences

In the case above on soil pollution, centralisation seems, at first sight, contrary to basic economic logic. From an economic point of view, the environmental clean-up standards to be provided could differ according to differing preferences of citizens.[100] Again, from an economic point of view, there is no reason for centralisation if the externalities are local and no prisoners' dilemmas exist. This economic argument in favour of differentiation according to the preferences of citizens is not only valid for the question whether or not the Greek turtle should be protected at the European level.[101] It is also valid for the whole body of environmental law, and even for environmental liability standards. This corresponds with the Tiebout framework of competition between legal orders where citizens are free to choose the environmental quality that corresponds optimally with their preferences. The consequence of this economic approach is that it should be for Greece to decide whether to prefer economic development or environmental quality.[102] A consequence of this economic argument whereby citizens choose a level of environmental protection according to their preference should obviously be that the environmental quality would vary according to the individual preferences of citizens. This argument is also used at the normative level in the United States, where there are increasingly pleas in favour of standard-setting by the states rather than by a federal environmental agency.[103] This *economic* argument therefore leads to an environmental federalism in which environmental quality between Member States could differ as long as there are no transboundary effects and no 'race for the bottom' risks.[104] For areas related to environmental liability such as soil pollution this would mean that states would be free to choose their own clean-up and liability standards.

Guaranteeing a basic environmental quality

There is, however, an important legal or policy argument that could lead to centralisation. This has to do with the idea of guaranteeing all European citizens a similar environmental quality. This is sometimes referred to as the protection of the 'European environmental and cultural heritage and human health'. If this argument is accepted at the policy level, it could be used to harmonise environmental quality. It is, however, important to note that the reason for centralisation in such a case would then not be the economic need of market integration, but the

96 W. Wils, 'Subsidiarity and the E.C. Environmental Policy: Taking People's Concerns Seriously', [1994] JEL at 85 to 90.

97 Compare D. Esty, 'The health of ecosystems to which we have no physical connection may enter directly into our utility calculus', Note 40 above at 592 to 596 and 640.

98 Compare A. Ogus, Note 35 above, at 418, who argues that harmonisation may be justified if foreigners derive disutility from observing the plight of victims in the offending state.

99 But then the Greek should probably be compensated for the extra costs involved in this European habitat protection (compare S. Rose-Ackerman, *Controlling Environmental Pollution. The Limits of Public Law in Germany and the United States* (1995), at 42 to 43).

100 Developed by A. Ogus, 'Standard Setting for an Environmental Protection', in M. Faure, J. Vervaele and A. Weale (eds), *Environmental Standards in the European Union in an Interdisciplinary Framework* (1994), at 25 to 30 and more generally in A. Ogus, Note 35 above, at 413.

101 To be very specific: this paper is not concerned with the normative question of whether or not the Greek turtle deserves protection. It is concerned only with the question whether such a decision should be taken in Greece or at the European Community level.

102 Again this is not to say that Greece should not protect the environment, but only to argue that from an economic point of view, this is not a question that Brussels should be concerned about.

103 D. Schoenbrod, 'Why States, not EPA, should set Pollution Standards', [1996] 4 *Regulation*, at 18 to 25.

104 However, since firms are in a competitive environment a Member State which chooses to impose a high level of protection (and thus high costs on firms) will have to compensate this with, say, lower taxes on wages in order to avoid the exit of business, so S. Rose-Ackerman, Note 99 above, at 41.

ecological desire to guarantee all citizens within the Union a similar, or at least basic, environmental quality. The consequence would then be that, contrary to economic logic, it would not be the preferences of citizens that would prevail, but the policy desire to provide one basic environmental quality in Europe.[105] This corresponds with the point made by Ogus that the preferences of citizens for lower standards at lower costs may sometimes be overruled if it is held that these low standards would infringe widely held perceptions of human rights.[106] In the environmental context this point could take the form of guaranteeing all citizens a basic environmental quality.[107]

Again this article does not argue at the normative level that this would not be a valid argument for centralisation, but it is important to stress that if this argument for centralisation is used, it is only for ecological (or policy) reasons, not for economic reasons, that one would strive for harmonisation of environmental quality. A problem with this 'European heritage' argument is that it may be valid to defend, for example, a European-wide protection of, say, the Coliseum in Rome,[108] but less so to guarantee a minimum environmental quality. In that case it would make more sense to strive for a Europe-wide minimum level of public health, which is not the case today.

But if this 'European heritage' reason for centralisation in order to guarantee all European citizens a basic environmental quality is accepted, there are several consequences. If externalities are merely local and no 'race for the bottom' risks exist, it is hard to find an economic rationale for centralisation. At the policy level, truly ecological reasons can be advanced for centralisation to guarantee a similar environmental quality throughout the union. This could take the form of minimum standards which should be achieved after the clean-up of polluted soils. But then this ecological argument, not the 'harmonisation of conditions of competition argument' has to be advanced to justify, say, the guarantee of a minimum environmental quality in Greece.[109]

Relating to environmental liability one can argue that this 'ecological' argument may be used to defend, for example, the European-wide protection of certain specific habitats.[110] However, this is not an argument to harmonise the liability rules that would have to be applied if damage is caused to such a habitat.

Balance

In this section, the economic literature on federalism has been used to provide a critical look at some aspects of the harmonisation of environmental law in general and environmental liability in particular. The economic arguments were also compared to the arguments advanced in favour of harmonisation in Europe. First there has been an attempt to provide an economic analysis of the traditional European argument that conditions of competition should be harmonised to 'create a level playing field'. This argument is too general to fit into the economic criteria for centralisation. This economic literature provides a balanced answer with respect to the types of subject-matters that should be regulated at the centralised or at the decentralised level. This shows that the questions concerning centralisation and harmonisation cannot be answered by black or white statements. From the economic literature it appears that there are very few economic reasons for harmonisation of environmental liability legislation. Such an argument would only exist if domestic polluters could externalise environmental damage to 'foreign victims'. However, other remedies may be available to cure interstate pollution without the need to harmonise liability. A second economic reason for centralisation would exist if it would be established that states could attract industry with lenient environmental liability standards. That is, however, very unlikely since states would, on the

105 Compare D. Esty, who argues in favour of global environmental norms which should represent a behavioral minimum (Note 40 above, at 570). More critical is R. Revesz, 'Federalism and Regulation: some generalizations', in D. Esty and D. Geradin (eds), *Regulatory Competition and Economic Integration. Comparative Perspectives* (2001), at 3 to 29.

106 'Rights may, in this instance, justifiably "trump" efficiency', so A. Ogus (Note 35 above, at 418). See also M. Cohen (Note 47 above, at 170) who calls for minimum quality standards at centralised level for reasons of 'equity, justice, or pure paternalism' and R. Stewart, who states that geographically uniform standards ensure every individual a minimum healthy environment even though such uniformity is economically inefficient (R.B. Stewart, 'Pyramids of Sacrifice? Problems of Federalism in Mandating State Implementation of National Environmental Policy', [1977] 86YLJ, at 1196 to 1272 and R. Stewart, 'Environmental Regulation and International Competitiveness', [1993] 102YLJ, at 2039.

107 See explictly C. Kimber, Note 21 above, at 1690: 'An analogy may be drawn here with human rights. It is arguable that certain minimum standards of environmental protection ought to be achieved by all countries and regions, particularly if one accepts that the environment is the common heritage of us all.'

108 But there it is the transboundary ('psychic') spill-over which justifies European intervention.

109 If the idea is accepted that it is for ecological reasons (harmonising environmental quality in the Union) that centralisation is needed, this has consequences for environmental standard setting. This point is further developed in M. Faure, Note 31 above, at 263 to 286.

110 So A. Arcuri, Note 40 above, at 41 and see R. Revesz, Note 65 above, at 22.

contrary, enact legislation to protect domestic victims of environmental pollution with high standard environmental liability legislation. There could be transaction costs savings of uniform environmental liability law if a Directive could create legal certainty and achieve full harmonisation, which is highly doubtful with the regime proposed in the White Paper.

Nevertheless, some non-economic arguments like ecological reasons, for example the guarantee of a high environmental quality in the European Union, might be legitimate arguments for a certain amount of harmonisation and centralisation.

Therefore the question that should be asked is what the goal of harmonisation of environmental law should be. If European environmental policy is, as is sometimes stated, to promote uniform environmental quality within the Union, this can be reached by fixing a harmonised environmental quality, to be enforced by the Commission, but with differentiated legislation for example on environmental liability. If the goal of environmental policy is to equalise conditions of competition, hence purely economic, it should be examined whether harmonisation of environmental liability legislation really improves equal competition, or whether it serves some industries that lobbied to erect artificial barriers to entry. That issue will be addressed below when we examine the importance of special interest.

EUROPEAN ENVIRONMENTAL LIABILITY REASSESSED

This section closes the circle and goes back to the starting point of this article, the Commission's White Paper on Environmental Liability So far we have found that there are relatively few economic arguments in favour of centralised environmental liability rules. However, we have already indicated that, within the framework of the subsidiarity discussion, the European Commission advanced arguments to justify a European wide environmental liability regime. These arguments put forward by the Commission for an EC environmental liability regime (see above) will now be confronted with the economic criteria for centralisation presented above.

Transfrontier Damage

The first argument of the Commission dealt with transboundary damage. It is held in the White Paper that Member States cannot effectively address cross-border pollution. Indeed, as the literature on federalism indicates, the Tiebout model will not yield efficient results when cross-border externalities are not adequately addressed.[111] In the case of cross-border externalities, the EC and not the Member States should have jurisdiction.[112] This cross-border rationale, however, provides an explanation for only part of the EC environmental legislation, as the EC acknowledges implicitly: 'the Union's current policies extend far beyond air and water quality to include the protection of soils, habitats and fauna and flora, and the conservation of wild birds'.[113]

However, if cross-border harm is a serious problem in the EC but Member States can adequately deal with pollution within their borders, then according to the subsidiarity principle, an EC liability regime would only be justified for cross-border environmental harm instead of an overall liability regime. This would result in a so-called 'transboundary only' regime. In this respect, liability for environmental damage is different from other areas of tort like product liability. Products cross borders all the time, but habitats stay where they are.[114] Moreover, according to Bergkamp, cross-border externalities by themselves do not necessarily require a harmonised liability regime: 'additional regulatory initiatives or more effective enforcement mechanisms might cure these as well'.[115] Indeed, case law in many Member States has developed in order to allow an extraterritorial application of domestic law on cross-border pollution. These jurisprudential evolutions may thus cure cross-border externalities without the need for a total harmonisation of environmental liability.

To summarise, transboundary environmental pollution can occur in certain cases in the EU. However, this argument by itself is not sufficient for a fully harmonised liability regime in the EU. Other remedies may cure this problem. Moreover, even if harmonisation were to be considered a preferred legal instrument it could only justify a European 'transboundary only' regime and not a total harmonisation.

The Polluter Pays Principle

An argument which seems to be very important for the Commission is the polluter pays principle. The Commission believes that environmental liability may encourage investment in research and development (R&D) for improving knowledge and technologies. What can be said about this argument from an economic perspective?

111 M. Faure, 'Harmonisation of Environmental Law and Market Integration: Harmonising for the Wrong Reason?' [1998] *European Environmental Law Review* at 169 to 175.
112 L. Bergkamp, Note 8 above, at 107.
113 europa.eu.int/pol/env.info.en.htm
114 L. Bergkamp, Note 8 above, at 107.
115 Ibid.

First, it should be made clear that the polluter pays principle as such does not explain why environmental regulation should be issued at the European level to promote this principle. Indeed, in this respect we should refer to the whole range of regulations that exist already today in the Member States. The Commission offers no evidence that the liability regime as proposed will create more incentives for prevention than the existing national and European liability and regulatory schemes.[116]

Second, the White Paper's statement that the liability legislation will promote R&D is not supported by empirical evidence either.[117] According to economic theory, if no adequate intellectual property rights are available, R&D will to a large extent be a 'public good' which private parties will not produce, or produce insufficiently. The reason is that once the investment is made, all competitors will profit without having to make any research investments themselves. This is the well-known 'free rider' problem. Furthermore, the firms might have incentives not to invest in R&D because in the future, the outcome may become the minimum standard.[118]

Third, the polluter pays principle does not resolve the question of whether costs of pollution should be internalised through *ex ante* regulatory requirements, or through *ex post* liability rules. Nor does it resolve controversies like forcing innocent or marginal polluters to pay for damage caused by their predecessors, or that any polluter has to pay for unforeseeable or tolerable damage. In that case, liability is a way of making the polluter pay, but it might be a very unattractive option and even economically inefficient.[119]

Therefore, the polluter pays principle does not explain or justify, at least from an economic perspective, the need for European action.

Decontamination and Restoration of the Environment

The Commission repeatedly expresses its expectations that a liability regime would encourage decontamination and restoration of the environment and improve the implementation of EC environmental legislation.[120] This consists in fact of a variety of sub-arguments. First, it is argued that a European regime would encourage the restoration of the environment.

Although one could only cheer this result, these expectations are probably more idealistic than realistic. Liability is neither a sufficient nor a necessary instrument for realising these objectives.[121] Bergkamp points out that the argument that an EC liability regime is necessary to ensure the restoration of damaged habitats is not sufficient, as Member States are already requested to do so.[122] He suggests that, if the objective of an EU environmental liability regulation is the remediation of contaminated land, then EC law should solely impose an obligation on Member States to reach this objective. Consequently, the Member States will be free to choose the instruments they will use. This may, but does not have to involve additional liability rules.[123] According to Bergkamp, 'liability is not the right instrument to promote compliance with environmental regulations, unless it is used as a sanction for damage caused by non-compliance and the regulatory compliance defence is fully recognised.'

In the section on criteria for centralisation, we have already pointed out that there are few economic reasons that can be advanced for a harmonised liability regime. However, we indicated that non-economic reasons, like the European heritage argument, might suggest some European action. However, if the Commission refers with the 'decontamination and restoration' argument to the desire to guarantee all European citizens a similar (high) environmental quality, this objective might be fulfilled by some means other than environmental liability. Whereas liability punishes industry, market-oriented approaches encouraging R&D in greening the industry (by funding), combined with clear clean-up standards for the Member States, might be more effective.

Second, the argument is made that by using liability law the implementation of EC environmental legislation can be promoted. But as just indicated, European law provides for a wide variety of other legal instruments to stimulate implementation of European law. Liability rules can only play a minor role to that effect.

Third, it should be stressed that the Commission apparently does not propose a European-wide harmonised environmental liability regime, but links the EC liability regime with existing EC environmental legislation. Moreover, the Commission specifically focuses the proposed regime on damage to biodiversity since most

116 Ibid., at 108.
117 Ibid.
118 C.D. Kolstad, *Environmental Economics* (2000).
119 M. Faure, 'Economic Aspects of Environmental Liability: An Introduction', [1996] *European Review of Private Law* (ERPL) at 90 and L. Bergkamp, Note 8 above, at 108.
120 *White Paper on Environmental Liability*, § 3.1–3.2, at 14.
121 L. Bergkamp, Note 8 above, at 108.
122 Council Directive 92/43 on the conservation of natural habitats and wild fauna and flora, OJ L206 at 7.
123 L. Bergkamp, Note 8 above, at 108.

existing Member States' environmental liability regimes would not cover this type of damage.[124]

From a subsidiarity perspective, this approach seems to be rather balanced in that it focuses merely on those areas where Member States have apparently not enacted legislation and limits itself largely to liability resulting from activities regulated under EC environmental law. However, several objections could be made against this approach as well. First, the mere fact that Member States have not enacted legislation with respect to a particular subject-matter is obviously, under subsidiarity, no justification for a European intervention. Second, it simply does not seem correct that the White Paper would merely deal with areas where Member States have not yet enacted legislation. The White Paper, for example, deals extensively with soil pollution within Member States. Finally, although the balanced approach of not opting for a total harmonisation can be defended (although it would have been better to limit the European regime to transboundary damage), one disadvantage is obviously that it has become so complex that the differences in conditions of competition will obviously remain in existence. This shows once more that any approach which chooses to combine European and Member State legislation can never lead to a 'level playing field', so that argument can not justify European competences.

Creation of a Level Playing Field

Although the Commission does not put the argument on the creation of a level playing field in first place in its White Paper, it probably will be one of the main arguments for harmonisation.

The literature on federalism, however, clarified that the risk of a 'race to the bottom' is very unlikely to occur in the EU. Even if differences in the stringency of environmental law exist between Member States, this will generally not lead companies to relocate to 'pollution havens' within Europe. This argument has been extensively dealt with above.

Moreover, full harmonisation can not be justified either in order to create 'equal conditions of competition'. The reasons have been discussed above. The Commission from its side also admits that there is no clear evidence of this advantage. Moreover, studies carried out at the request of the Commission have shown that the effect of liability regimes on competitiveness remains unclear.[125] The Commission admits in the White Paper that 'no significant impact is discernible and the environmental liability regimes in place in Member States ... have not led to any significant competitiveness problems'.[126]

If that is the case, one may wonder how an EC Directive can be justified on the premise of levelling the playing field. Moreover, the White Paper stipulates that the Directive should be based on Article 175 of the Treaty. Article 176 provides notably for Directives based on Article 175 that Member States would be authorised to go beyond the Directive's scope and broaden it.[127] Therefore grounds of competitiveness cannot justify EC intervention. Bergkamp rightly indicates that in these circumstances any competition distortions that may exist would be likely to persist even after the proposed liability regime is implemented.[128]

Moreover, we indicated that the regime proposed in the White Paper is so complex that it can never have the effect of creating a 'level playing field'. The argument of the creation of a level playing field is therefore not sufficient to allow for a harmonised European environmental liability regime.

Principle of Equal Treatment

The final argument dealt with is the principle of equal treatment. The equal treatment is discussed in the White Paper in the context of the transboundary externalities argument.

In the literature it has been suggested that if interstate externalities are a reason for centralisation, the European Directive should not necessarily cover both local and community-wide pollution.[129] This idea of a 'transboundary only' regime was rejected, since this could lead to inequalities in the treatment of victims in Member States depending on whether they were victim of a transboundary or a local pollution.[130] Nevertheless this White Paper on environmental liability shows that the Commission recently (the White Paper was issued on 9 February 2000) seems to

124 For a critical perspective of the European competence with respect to environmental liability see G.J. Niezen, 'Aansprakelijkheid voor milieuschade in de Europese Unie', in *Ongebonden Recht Bedrijven* (2000), at 165 to 167 and 168 to 169.

125 'Economic aspects of liability and joint compensation systems for remedying environmental damage, summary report', ERM Economics, London, March 1996 (annex to the White Paper).

126 *White Paper on Environmental Liability*, § 7, at 29.

127 *White Paper on Environmental Liability*, § 6, at 28. Article 176 provides that 'the protective measures adopted pursuant to Article 175 shall not prevent any Member State from maintaining or introducing more stingent protective measures. Such measures must be compatible with this Treaty. They shall be notified to the Commission.'

128 L. Bergkamp, Note 8 above, at 106.

129 Van den Bergh suggested that a distinction should be made between regional and interstate pollution (Note 46 above, at 10).

130 *White Paper on Environmental Liability*, at 25 to 26.

be aware of the arguments advanced in economic literature in favour of (de)centralisation and at least discusses them.

Strikingly, the White Paper, at least implicitly, discusses the criteria advanced by economic analysis for centralisation at the European level (more particularly the transboundary character of environmental pollution and the 'harmonisation of conditions of competition' arguments) and rightly points to the fact that these arguments would theoretically lead to a preference for a 'transboundary only' regime. The White Paper, however, rejects this approach on the basis of the mentioned equality arguments.

Bergkamp indicates that when referring to equality, the Commission no longer argues within the scope of the subsidiarity principle, but simply pleads for uniformity.[131] As we will argue in the next section, this argument could fit into the public choice theory which holds that industry in heavily regulated (and probably polluted) areas lobbies (supported by green NGOs) to force their very stringent environmental regulations upon other Member States that might not need such stringent measures. In that way, this industry might erect artificial barriers to entry.

Yet the subsidiarity principle has been included in the EC Treaty precisely to prevent European action justified mainly on a request for uniformity, possibly by industry in heavily regulated areas.[132] As mentioned above, the subsidiarity principle allows the Community to take action if and only in so far as the objectives of the proposed action cannot be sufficiently achieved by the Member States. As it is not proven that uniformity is necessary for the Member States in order to deal effectively with environmental damage, there is no need for full harmonisation. The equality argument is hence not very convincing, neither from an economic, nor from a legal perspective.

PUBLIC CHOICE CONSIDERATIONS

So far we have discussed the economic criteria for (de)centralisation, applying these to the area of environmental liability. We compared them to the arguments advanced by the European Commission to justify European competences, as they were advanced in the White Paper.

We concluded that relatively few economic arguments can be found to justify centralisation in the area of environmental liability. This was only the case for transboundary pollution and even then the question arises whether the same result cannot be reached through different, less far-reaching legal instruments than total harmonisation.

Nevertheless, we found that there are apparently strong forces in Brussels striving for a European environmental liability regime, at least for damage to biodiversity. To some extent this can still be explained on public interest grounds since we also indicated that non-economic, ecological arguments could be advanced to strive, say, for a minimum quality of clean-up for polluted soils. However, public choice scholars have thought that there is always a risk that regulation in fact serves the interests of particular pressure groups.

Indeed, another non-economic reason why the European Union should harmonise liability legislation can be found in public choice theory. Public choice theory deals with the role of interest groups in legislation. Lobbying activities at the European level are extremely strong. With respect to environmental standard-setting, intensive rent-seeking behaviour by interest groups can be identified. In Europe, industry may be confronted at state level with 'green' non-governmental organisations (NGOs), whereas these countervailing powers might have less force in Brussels. Moreover, the lack of transparency in the decision-making process, with which the European Union is often reproached, will stimulate European industry to engage in serious lobby efforts.

The lobbying does not necessarily have to result in lower environmental standards. In particular cases, special interest groups, representing industry, might, understandably, lobby in favour of harmonisation at a higher level of environmental protection.[133] Interest groups in areas which are already heavily regulated may have incentives to extend their strict (national) regulations to the European level, forcing foreign competitors to follow the same strict regulation with which they already comply. The result is that industry will lobby to erect artificial barriers to entry. In addition, green NGOs will be pleased with this lobby and will obviously support the demand to transfer strict national standards into a European standard.[134] Thus, industry in heavily regulated (and probably polluted) areas can (supported by green NGOs) force their very stringent standards on their (southern) competitors, although these Member States probably would not need these stringent standards if the policy goal were one of reaching uniform environmental quality.

131 L. Bergkamp, Note 8 above, at 107.
132 Ibid.
133 See also D. Esty and D. Geradin, Note 44 above, at 303.
134 These 'alliances' between environmentalists and domestic producers are also discussed by D. Vogel, Note 67 above, at 52 to 55.

Thus it becomes clear that the 'harmonisation of conditions of competition' argument is used to serve the interests of industries in heavily regulated areas to erect barriers to entry. Hence, environmental law can be used to limit market entry and environmental law is abused to serve private interest goals.

This leads to the conclusion that 'harmonisation of conditions of competition' argument, as presented in European rhetoric, can even be problematic, from both the economic and ecological points of view, and in fact serves the interests of industrial groups in heavily regulated areas.[135] It can be in their interests that 'conditions of competition' are actually harmonised.

It is not clear yet whether the White Paper on environmental liability should be considered as an attempt by interest groups to create barriers to entry. One problem is that the contents of the White Paper are still rather vague and specific details of the regime (such as clean-up standards) are not yet known.

The Commission argued that the White Paper deals with a topic, damage to biodiversity, which has yet not been the subject of legislation in the Member States. That is, however, only partially the case. Most Member States may indeed lack specific rules, for example concerning the way damage to natural habitats has to be calculated. But the White Paper also addressed the area of soil pollution, for which extensive regulations exist in most Member States. Thus theoretically one could still run the risk that industry in Member States with stringent soil clean-up regulations would strive for centralisation, thus creating a barrier to entry for competitors from countries where these strict standards do not yet apply.

It is too early to assess whether the desire to create a European environmental liability regime in fact serves the interest of industry. One should, however, always be aware of the fact that this risk, that centralisation is abused to create barriers to entry, may appear in any attempt at centralisation.

POLICY RECOMMENDATIONS AND CONCLUSIONS

This article has tried to examine whether there are economic reasons for the harmonisation of environmental liability legislation in the European Union. The arguments brought forward by the Commission in its White Paper on Environmental Liability have been examined, in particular the traditional European argument that a harmonisation of conditions of competition would be necessary, in order to create a level playing field. The literature on federalism makes it clear that there are very few economic arguments to justify a harmonised liability regulation in the European Union. Even though there may be an argument for centralisation in case of transboundary pollution, this does not justify a total harmonisation of environmental liability. Also the other economic argument in favour of harmonisation, the 'race for the bottom' argument, does not seem to be valid in the current European context. There is no empirical evidence at all that current European Member States would have engaged in a race for the bottom as far as inefficient environmental liability law is concerned. Note, however, that this argument may be different if, after enlargement, one would look at the particular situation of Eastern Europe. There the race for the bottom, the risk that some Member States would engage in destructive competition, could be realistic. But then the question could still be asked whether harmonising environmental liability law would be an appropriate remedy for that risk.

It should equally be examined whether a total harmonisation of liability standards is needed to reach a common market in Europe. Other useful but not that far-reaching (less inefficient) instruments may be available. One can think, for example, of a standardisation of procedures within environmental law, which still remains useful because of the transboundary character of pollution and industrial operations.[136] This can indeed increase transparency, as was intended to be achieved by the IPPC Directive, and can reduce transaction costs. However, such a harmonisation should not necessarily be achieved through formal Directives, but can also be achieved through a search for common principles through comparative research, looking for a *ius commune*.

Therefore, the basic question the European Union should ask is what the goal of harmonisation of environmental liability should be. European policy-makers should think more thoroughly about the reasons for harmonisation or at least about the rhetoric used to justify such a harmonisation. More particularly they should realise that they can either opt for the ecological goal of uniform environmental quality or for the goal of harmonising legislation, but not for both at the same time. One now has

135 This is not to say that there is no risk of regulatory capture resulting in inefficient standards at the level of the Member States: compare (in the US context) S. Rose-Ackerman, Note 32 above, at 166 and 173. However, in Europe, it is especially the non-transparent Brussels bureaucracy which is feared from a public choice perspective.

136 This is suggested by D. Esty and D. Geradin, Note 44 above, at 293.

the impression that the instruments chosen (harmonisation of legislation) do not always match with the expressed goals (harmonisation of environmental quality). Apparently also European legal scholars are coming to this insight as well. Recently De Witte argued that Europe should now leave the (wrong) rhetoric about harmonisation of conditions of competition aside and should clearly state that it wants to achieve a minimum quality for its citizens.[137]

Therefore, the reader should again be aware that in this article we merely provided 'one view of the cathedral'. We merely addressed the question whether a harmonisation of environmental liability is needed for economic reasons. That question is justified since the European Commission itself advances an economic reason (harmonisation of marketing conditions) to justify European action. That reason is, so we tried to show, particularly weak and the same is the case for other reasons advanced by the Commission. The conclusion at the normative level is, however, not necessarily that there should be no European action at all with respect to environmental liability. Our main problem is that the Commission still seems to be stuck in the old integration jargon of 'harmonisation of conditions of competition', whereas that seems to be a weak reason for harmonisation. There may be other, non-economic reasons to justify a harmonisation. One could simply be the fact that one may hope that action at the European level with respect to biodiversity damage might lead to a better protection of biodiversity than the absence of European action. To some extent this argument is also made in the White Paper. But our point is that the Commission should then be clear and open about the goals it precisely wishes to achieve with action at the European level. In that case, an *ex ante* effectiveness test could also be executed to examine whether the method of harmonisation chosen in the White Paper could lead to the goals it wishes to serve. In other words, the definition of a particular goal of harmonisation may have consequences for the contents of the liability regime chosen as well. Therefore it is not at all unimportant to address this subsidiarity issue carefully.

This issue remains important even though the Commission has now apparently advocated a different approach from the one followed in the White Paper by focusing more on prevention and restoration of significant environmental damage. Even if a future European regime focused more on a duty to restore, the question why and how this should be dealt with at the European level remains important.

In that respect it should be stressed that economic analysis of federalism provides certainly useful insights concerning the question of centralisation, but it does not always provide an answer to the question which of the many possible legal techniques of harmonisation has to be chosen to deal with a particular problem. The economic notion of *centralisation* is too general to cover all the legal techniques of *harmonisation*. It therefore certainly merits further research as to which of these harmonisation techniques is best suited to deal with a particular problem like environmental liability. Moreover, also in the economic analysis there are unanswered questions which merit further research. One of them is how the need to centralise decision-making in case of transboundary externalities can be reconciled with the ecological goal of a uniform environmental quality. Another is whether industry in heavily polluted areas may be disadvantaged with more stringent standards compared to their competitors in 'cleaner' countries. Some of the questions need further empirical research, for example into the influence of environmental regulation on industry behaviour. In that respect Europe should certainly carefully look at the US experience with environmental federalism.[138]

137 B. De Witte, 'Carving out a Place for European Union Law in the Legal Universe' (paper presented at the conference Ius Commune in a World Context, Maastricht 15 April 1999, forthcoming in the *Maastricht Journal of European and Comparative Law*).

138 See for comparative analyses of environmental federalism in the United States and Europe, C. Kimber, Note 21 above; D. Esty and D. Geradin (1998) and (1997), Note 44 above; J. Pfander, 'Environmental Federalism in Europe and the United States: A Comparative Assessment of Regulation through the Agency of Member States', in J. Braden, H. Folmer and T. Ulen (eds), *Environmental Policy with Political and Economic Integration, The European Union and the United States* (1996) at 62 to 75 and S. Rose-Ackerman, Note 99 above, at 37 to 54.

Appendix: White Paper Liability Regime

Proposed EU regime

Possible scope of an EC environmental liability regime